

**Testimony of the Michigan Chamber of Commerce
Before the House Tax Policy Committee
Wednesday, November 29, 2005
Examples of Double Taxation Presented by Sue Kinney-Huffman**

Thank you for allowing us to take a few minutes of your time to explain our concerns regarding the application of both sales **and** use tax, resulting in double taxation to Michigan businesses. As Tricia mentioned in my introduction, the information and examples I will share with you relate to personal experience as a former auditor for the Michigan Department of Treasury (Treasury), a consultant defending clients while in public accounting, and the insight gained working with private industry. We all agree that taxes are a "fact of life" - however, double taxation is unfair.

The State of Michigan is a "vendor" (retailer/seller) liability state, meaning that while retailers have the ability to pass along sales tax to consumers, the retailer is still liable for the collection and remittance of the tax if an exemption from the tax is not applicable.

Historically, Treasury conducted audits of Michigan vendors for accurate collection and remittance of sales tax. However, within the past couple of years the focus has shifted from a *sales tax audit* of the vendor to a *use tax audit* of the purchaser. For those unfamiliar with use tax, it is typically viewed as complimentary to the sales tax. It is the same rate (6%) and is applied to the storage, use or consumption of tangible personal property and some services in the state of Michigan. Treasury has cited the adoption of the Streamlined Sales Tax Agreement as the reason for the shift in audit focus from the seller to the purchaser.

The purpose today is to provide you with examples of double taxation that I have experienced first hand while representing former clients under audit.

Retailer not required to separately itemize sales tax. Many of you are familiar with an invoice provided by an individual that repairs an item in your home and "lump sum bills" (labor, parts and tax) the amount due. The same type of billing can occur in business- to- business transactions. The manner in which the invoice is presented to the purchaser is not incorrect. The service provider can statutorily invoice in this manner.

However, because sales tax is not separately itemized - under current audit policy - this invoice would be taxed again.

Credit Card / Pro Card Purchases: The situation is very similar with employee reimbursements. Company issued credit card statements are reviewed in detail and supporting documentation of tax paid must be provided. Most credit card statements do not provided line item detail which verifies tax was paid. Again, the tax may have been paid but Treasury makes the automatic assumption that it has not been paid.

Projection of the audit deficiency: We need to keep in mind that the items have the potential of being taxed numerous times. Most audits are conducted using a sample which is projected over a four year statutory period. A transaction on which sales tax was applied at the time of purchase and included in a sample based on a quarter of a year has the potential to be taxed 16 more times.

Application of Penalty and Interest: There are provisions in the statute for the application of penalty and interest. The application of penalty and interest to transactions which were properly taxed at the time of sale (or purchaser) is a concern.

Record retention: The shift of focus from the vendor, who is required to collect and remit the tax, to the purchaser has created a hole in record retention. Many business-purchasers are unaware of the change in audit focus. As a result, providing documentation for already taxed transactions is not possible.

Retroactive vs. prospective application: In addition to the problems with adequate record retention, we must examine the application of this change in focus from the vendor to the purchaser. The change of focus has not been properly communicated to taxpayers yet the audit procedures are being applied retroactively.

Administrative burden. In addition to double taxation, an administrative burden is placed not only upon the taxpayer but onto audit staff as well. The taxpayer is now required to retain documentation that was not previously required. Treasury runs the risk of being to forced to rework audits. For example, a use tax audit completed on a taxpayer results in a deficiency which includes a taxable transaction that is later determined to have already been taxed by the vendor. The taxpayer has one year from the date of completion of the audit to protest the findings. In this scenario, the auditor who

completed the audit would be required to recalculate the audit deficiency and Treasury would be forced to pay a refund for the overpaid tax.

Interpretation of the Statute: One final point that may not necessarily be related to double taxation but does create audit problems for the purchaser is the interpretation of the statute. As previously noted, it is the vendor's (retailer/seller's) responsibility to collect and remit the tax. Situations have occurred where the vendor did not properly interpret the sales tax statute. When the focus is placed on the purchaser the end result is that the purchaser remits tax under audit (which was properly due) and the applicable interest. Had the seller properly interpreted the statute, the purchaser would have paid the sales tax at the time of purchase and not the additional interest.

Isolated Transactions: Another area in which Treasury has shifted its focus is the taxation of isolated or "one-time" transactions. For example, a manufacturing company sells its used copy machine to another manufacturer. Under prior audit and statutory guidelines this was considered an isolated transaction ...similar to a neighborhood garage sale. Under today's audit guidelines this becomes a transaction subject to sales/use tax.

Cross reference of audits of sellers and purchasers: Some states have the ability to cross reference audit work papers between sellers and purchasers so that double taxable does not occur. Unfortunately, Michigan does not have this capability.

Closing: I would like to close by stating the examples provided here are merely a sample of some of the problems Michigan businesses have tolerated. We would like to work with you (our legislators) and Treasury to arrive at a fair method of auditing and the like.

THANK YOU again for your time.